LIBRARY
SUPREME COURT, U.S.

Office - Supreme Court, U. S.
FILED
JAN 23 1956
HAROLD B. WILLEY, Clerk

No. 255

In the Supreme Court of the United States

OCTOBER TERM, 1955

MILLINERY CENTER BUILDING CORP., PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT

SIMON E. SOBELOFF,
Solicitor General,
H. BRIAN HOLLAND,
Assistant Attorney General,
RALPH S. SPRITZER,
Attorney to the Solicitor General,
A. F. PRESCOTT,
LOUISE FOSTER,
Attorneys, Department of Justice,
Washington 25, D. C.

INDEX

	Page
Opinions below	1
Jurisdiction	1
Questions presented	2
Statute involved	2
Statement	3
Summary of argument	6
Argument:	
I. No portion of the sum paid under the purchase agreement can be deducted by the taxpayer as an ordinary and necessary business expense	8
II. The Court of Appeals correctly held that the portion of the purchase price allocable to the building is to be depreciated over the period of the building's remaining useful life	18
Conclusion	21

CITATIONS

Cases:

Bell v. *Harrison*, 212 F. 2d 253	20
Bonwit Teller & Co. v. *Commissioner*, 53 F. 2d 381, certiorari denied, 284 U.S. 690	20
Boos v. *Commissioner*, 30 B.T.A. 82	12
Cassatt v. *Commissioner*, 137 F. 2d 745	13, 20
Cleveland Allerton Hotel v. *Commissioner*, 166 F. 2d 805	8, 12
Commissioner v. *Moore*, 207 F. 2d 265, certiorari denied, 347 U. S. 942	17
Commissioner v. *Stuart Co.*, 195 F. 2d 176	16
Denholm & McKay Co. v. *Commissioner*, 2 B.T.A. 444	13
Friend v. *Commissioner*, 119 F. 2d 959, certiorari denied, 314 U.S. 673	17

Cases—Continued

	Page
Heller, Clara Hellman, Trust No. 7610 v. Commissioner, 7 T.C. 556	20
Herzberg v. Alexander, 5 F. Supp. 334	12
Hort v. Commissioner, 313 U.S. 28	13
Hotel Kingkade v. Commissioner, 180 F. 2d 310	12
Lomas & Nettleton Co. v. United States, 79 F. Supp. 886	16
Miller v. Commissioner, 10 B.T.A. 383	20
Olympia Harbor Lumber Co. v. Commissioner, 30 B.T.A. 114	17
Post v. Commissioner, 109 F. 2d 135	12, 20
Willcuts v. Minnesota Tribune Co., 103 F. 2d 947, certiorari denied, 308 U.S. 577	12

Statute:

Internal Revenue Code of 1939, Sec. 23 (26 U.S.C. 1952 ed., Sec. 23)	2, 9, 19

Miscellaneous:

4 Mertens, Law of Federal Income Taxation, Sec. 25.20	12
48 Col. L. Rev. 965	13

In the Supreme Court of the United States

OCTOBER TERM, 1955

No. 255

MILLINERY CENTER BUILDING CORP., PETITIONER

v.

COMMISSIONER OF INTERNAL REVENUE

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT

OPINIONS BELOW

The opinion of the Tax Court (R. 1-15) is reported at 21 T.C. 817. The opinion of the Court of Appeals (R. 16-19) is reported at 221 F. 2d 322.

JURISDICTION

The judgment of the Court of Appeals was entered on April 14, 1955. (R. 20.) A petition for rehearing (R. 20-28) was denied on May 18, 1955. (R. 29.) The petition for a writ of certiorari was filed on July 22, 1955, and was granted on October

10, 1955, limited to questions 1 and 2 presented in the petition for the writ. (R. 29-30; 350 U.S. 820.) The jurisdiction of this Court is invoked under 28 U.S.C., Section 1254.

QUESTIONS PRESENTED

The order granting certiorari (R. 29-30) limits review to questions 1 and 2 presented in the petition for a writ of certiorari, which read as follows:

"1. Where a lessee, the owner of a valuable building on leased land, acquires the fee to the land to be relieved of what it considers to be the burdensome terms of a lease, may the lessee deduct the excess of the payment over the determined value of the land at the date of purchase as an ordinary expense of doing business under Section 23 (a) of the United States Internal Revenue Code of 1939 or under Section 23 (f) as a loss on a transaction entered into for profit and not compensated for by insurance or otherwise?

"2. In the alternative, may the lessee-petitioner consider the excess payment over the determined value of the land to be in the nature of a prepayment of rent for the remaining term of the extinguished lease and amortize such amount over 21 years?"

STATUTE INVOLVED

Internal Revenue Code of 1939:

SEC. 23. DEDUCTIONS FROM GROSS INCOME.

In computing net income there shall be allowed as deductions:

(a) [as amended by Sec. 121 of the Revenue Act of 1942, c. 619, 56 Stat. 798] *Expenses.*—

(1) *Trade or business expenses.*—

(A) *In general.* All the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business * * *

* * * * * *

(f) *Losses by Corporations.*—In the case of a corporation, losses sustained during the taxable year and not compensated for by insurance or otherwise.

* * * * * *

(l) [as amended by Sec. 121 of the Revenue Act of 1942, *supra*] *Depreciation.*—A reasonable allowance for the exhaustion, wear and tear (including a reasonable allowance for obsolescence)—

(1) of property used in the trade or business, or

(2) of property held for the production of income.

* * * * * *

(26 U.S.C. 1952 ed., Sec. 23.)

STATEMENT

The pertinent facts as found by the Tax Court are as follows:

Taxpayer leased land in New York City on April 30, 1924 and in accordance with the terms of the lease it erected a 22-story loft building at a cost of $3,000,000. Title to the building, improvements and fixtures belonged to taxpayer but was to vest in the landlord, at the expiration of the last term of the lease, at the option of the landlord. In the event of the destruction of the building by fire or other causes, taxpayer could not abandon the lease and was required to restore the building at its own cost. At the expiration of the lease or any renewal period, taxpayer was to surrender the premises and the building to the landlord at his option, free and clear of all encumbrances, without the landlord being obligated to pay for such property. (R. 4.)

The Commissioner had allowed taxpayer, during the 21-year term of the original lease, the entire cost of the building in annual depreciation deductions. (R. 13-14.)

Taxpayer had the option to renew the lease for two successive 21-year periods and did renew its lease, on April 16, 1945, for another 21-year period. (R. 4-5). Under the lease, the ground rent for the renewal period was fixed at six per cent of the value of the land as of the termination date of the prior term, but was to be no less than the previous rental of $118,840. The value of the land was to be determined as if vacant and unimproved, and the rent at six per cent of the value of the land in May 1945 would have been less than $100,000. (R. 5.)

On May 11, 1945, taxpayer entered into an agree-

ment of sale with Wendel Foundation, the owner of the land. Taxpayer purchased the fee and obtained release from the obligations of the renewed lease for $2,100,000. Taxpayer purchased the fee with a view to securing release from the terms of the lease. It was most concerned about the annual rental of $118,840, which it deemed excessive, and about the contingent liability to remove the building from the premises at the expiration of the lease upon the request of the landlord. (R. 5.)

Title to the land was taken by taxpayer on June 11, 1945. (R. 5). On the same day, the agreement of cancellation of the lease was also executed. (R. 6.) The value of the land, vacant and unimproved, was $660,000 as of the time of the purchase. (R. 8.) Taxpayer also incurred legal fees aggregating $16,500 in connection with the transaction. (R. 8.)

The Tax Court held (R. 9-15): (1) that taxpayer was not entitled to deduct any part of the sum of $2,100,000 paid under the 1945 agreement, or any part of its legal fees, as a business expense; (2) that taxpayer could not amortize any part of the purchase price over the 21 years during which the renewed lease would have been in force if it had not been cancelled; and (3) that taxpayer was not entitled, for purposes of depreciation deductions, to treat any part of the sum paid under the agreement as an addition to the cost of the building.

The Court of Appeals agreed with the Tax Court on the first and second points. It held, however, on the third point, that taxpayer, in purchasing

the fee, had acquired a reversionary interest in the building; that it was accordingly entitled to allocate a portion of the purchase price to the building; and that the sum so allocated could be depreciated during the remaining economic life of the building. The Court of Appeals found that it could not determine how much of the purchase price should be allocated to the buildings, since the record showed only the value of the land in its unimproved state. Accordingly, the cause was remanded for the Tax Court to determine the amount, representing additional cost of the building, which may be recovered through yearly depreciation deductions.[1] The Tax Court was directed to make a similar adjustment with respect to the legal fees incurred by taxpayer in connection with the purchase. (R. 16-20.)

SUMMARY OF ARGUMENT

I

In April 1945, taxpayer renewed, for a 21-year period, a lease covering land upon which taxpayer had previously erected (in accordance with the lease's requirements) a valuable building. Less than a month later, it bought out the landlord, extinguishing the lease. It thus acquired (1) fee title to the land and (2) absolute ownership of the

[1] Taxpayer assumes in most of its argument that the value of the land in its unimproved state (*i.e.*, $660,000) should be taken as its value on the date of purchase. The Court of Appeals found, however, that it was necessary, on the state of the record, to remand to the Tax Court for a determination of the land's value on the date of purchase. (R. 19.)

building which, under the lease, was to become the property of the landlord upon termination of the lease.

Both the fee to the land and the remaining property interests acquired in the building (which had a remaining useful life of 30 years) are capital assets of the classic variety. Taxpayer recognizes that the portion of the purchase price allocable to the land must be treated as a capital expenditure. But it would treat the balance as a payment made to escape an onerous lease, and it seeks to deduct this amount as an ordinary business expense of the year 1945. Apart from the fact that the rental fixed by the lease was not in fact found onerous, the argument is defective. Capital expenditures are frequently made by a business enterprise to eliminate recurrent expenditures or obligations which would otherwise have to be met. The acquisition of a capital asset is no less a capital expenditure because it has this effect. On the contrary, the hallmark of a capital acquisition is that the benefits derived therefrom will extend over a period of years. Whether viewed from the standpoint of savings incident to lease termination or from the standpoint of the productivity of the building acquired, it is plain that the benefits of this taxpayer's purchase will be realized over the course of years and that there is no sound basis, either in economics or in tax law, for attributing a disproportionate part of the purchase price to the year 1945. All of the authorities support this view with the exception of *Cleveland Allerton Hotel* v. *Commissioner*, 166

F. 2d 805 (C.A. 6th), a case which the courts below considered and believed to be unsound.

To the extent that the purchase price is allocable to the purchase of an interest in an exhaustible asset, *i.e.*, the building, the Court of Appeals has held that taxpayer may write off the expense by taking deductions for depreciation over the remaining useful life of the building. Taxpayer is plainly entitled to no more. It may not write off in one year a capital asset with a remaining life of many years.

II

Alternatively, taxpayer suggests that the portion of the purchase price allocable to the building should be depreciated over the unexpired term of the extinguished lease (approximately 21 years). But the effect of the purchase was not merely to end a contractual obligation having 21 years to run; taxpayer thereby acquired unlimited ownership of a building with a remaining useful life of 30 years. On ordinary principles of depreciation, incorporated in the Internal Revenue Code, the added investment which taxpayer made in the building in 1945 must be depreciated over the remaining life span of the building.

ARGUMENT

I

No Portion of the Sum Paid under the Purchase Agreement Can Be Deducted by the Taxpayer as an Ordinary and Necessary Business Expense

This case involves the proper tax treatment of a portion of the $2,100,000 paid by taxpayer under

the purchase agreement of May 11, 1945. Both courts below held that the entire sum of $2,400,000 was used for the purchase of capital assets and that, therefore, no part thereof could be deducted as an ordinary business expense. Taxpayer agrees that the amount paid for the land was a capital expenditure, and hence non-deductible, but it contends that a substantial sum ($1,440,000 or some other sum to be determined) was paid for the cancellation of the lease and that this sum should be deducted as an ordinary and necessary business expense under Section 23(a) of the Internal Revenue Code of 1939, *supra*, p. 3.[2]

Taxpayer's contention confuses the motive of the purchase with what was purchased. It ignores the fact that, by the payment of $2,400,000, it not only acquired fee title to the land, but also full ownership of the building which it had been required to erect and maintain under its lease. Prior to the purchase of the property, taxpayer's only interest was a right to possess the land as lessee and to hold title to the building as specified in the lease. The landlord, as the Court of Appeals held (R. 19), not only had title to the land but a reversionary interest in the building. This is plain from the terms of the lease. Thus, the lease states that at the expiration of the demised term (or other sooner ter-

---

[2] Taxpayer also asserts, in the alternative, that it is entitled to deduct the $1,440,000, or some determined sum, as a loss under 1939 Code Section 23(f), *supra*, p. 3, but does not argue the point. The courts below did not discuss it. It is apparent that, if the entire purchase price was a capital expenditure, this contention also falls. Accordingly, it will not be separately treated.

mination because of the lessee's default) title to the building and to other improvements and fixtures on the land shall, at the option of the landlord, vest in the landlord and its successors and become its "property free from any and all right, title or interest of the Tenant, its successors or assigns therein." (R. 37.) Moreover, in order to protect the landlord's interest, taxpayer was required to maintain the building in good condition at its own expense and, in the event of the destruction of the building in whole or in part, to rebuild that which was destroyed. At the expiration of the lease, it was the lessee's duty to surrender the premises and the building without any cost to the landlord. (R. 36-44.)

This situation was basically changed as a result of the purchase agreement. (R. 30-34.) Taxpayer, having certain rights in the property under the lease, thereupon bought up all remaining interests. It thus acquired not only fee title to the land covered by the lease, but also full ownership of a valuable building with a remaining useful life of 30 years. (R. 12.) As the court below said (R. 18), taxpayer is in the same position as if it had bought out the share of a co-owner, or an overriding easement, or a piece of land next door.

Because taxpayer also happened to be the lessee under the lease, its purchase resulted in the merger of the leasehold in the fee, and gave it a good bargain. But while that fact may explain in large measure the motivation for taxpayer's investment, it cannot change the fundamental nature of the

transaction: taxpayer was making a substantial investment to acquire capital assets of the classic variety—land and building.

Taxpayer's brief relies heavily upon the Tax Court's finding that taxpayer deemed the rental fixed by the lease excessive and was anxious to terminate that obligation. We note parenthetically that the Tax Court did not find (although taxpayer assumes) that the lease terms were in fact onerous or unreasonable, and that the Court of Appeals stated (R. 18) that the evidence in this respect was "doubtful at best." There is, in any case, a fundamental objection to taxpayer's assumption and to the arguments which are built upon it. It is almost invariably true that, when an operating business enterprise buys realty or adds to plant or productive equipment, it is motivated by the expectation of reduced costs and obligations over the course of future years. If a manufacturer decides to buy a fleet of trucks to carry his products in order to dispense with the necessity of patronizing common carriers, presumably he makes his decision in the expectation that the annual savings will more than compensate for the capital expenditure. This does not enable him to treat the capital expenditure as an "ordinary" expense incurred in lieu of meeting routine transportation charges. Indeed, it is the fact that the savings effectuated will be realized over the course of years, and not merely during the year of the outlay, which attests to the capital nature of the transaction.

It is, of course, a fundamental precept of tax

law that money spent to acquire income-producing property or property which will be of benefit to taxpayer's business in future years is a capital expenditure and not an ordinary and necessary business expense. *Willcuts* v. *Minnesota Tribune Co.*, 103 F. 2d 947, 951 (C.A. 8th), certiorari denied, 308 U. S. 577; *Hotel Kingkade* v. *Commissioner*, 180 F. 2d 310, 312 (C.A. 10th); 4 Mertens, Law of Federal Income Taxation, Sec. 25.20. Also, see *Herzberg* v. *Alexander*, 5 F. Supp. 334 (W.D. Okla.), and *Boos* v. *Commissioner*, 30 B.T.A. 882, holding that where a lessee acquires fee title to property covered by a lease before the cost of such lease is fully amortized he may not deduct the unamortized cost as a loss or business expense but must treat such amount as a capital expenditure. And cf. *Post* v. *Commissioner*, 109 F. 2d 135 (C.A. 2d), holding that a lessor-owner on selling property to a person who had previously purchased the lease covering such property from the lessee, could not deduct the unamortized cost of the lease as a business expense, but had to include such sum as a part of the cost of the property which was sold.

We submit that the conflicting decision in *Cleveland Allerton Hotel* v. *Commissioner*, 166 F. 2d 805, (C.A. 6th), which alone gives comfort to taxpayer, is erroneous.[3] The cases upon which the Sixth

[3] Both the court below and the Tax Court recognized that the *Cleveland Allerton* decision was inconsistent with the result reached in the instant case. In that case, the owner of a valuable hotel located on leased land bought the fee for $441,250 in the year 1941, extinguishing a 99-year lease which

Circuit relied, *Vassiff v. Commissioner*, 137 F. 2d 745 (C.A. 3d), and *Penfield & McKay Co. v. Commissioner*, 2 B.T.A. 444, are both clearly distinguishable. Neither of the lessees in those cases purchased the fee to the leased property. Each was seeking, and each secured, the cancellation of his lease for an agreed sum of money. Since each surrendered possession of the leased property, it is evident that neither acquired a capital asset.[4]

This distinction, which taxpayer would obliterate, is basic and rests on sound principles. Let us suppose, for example, that two businessmen, *A* and *B*, lease similar pieces of property, each for a term of ten years. After the expiration of a year, *A* decides that it is necessary to move this business to another location. Accordingly, he settles his obligation under the lease for an agreed sum and pays that sum to the landlord. *B*, on the other hand, decides, after a brief experience as lessee, that he wishes to make permanent use of the property in

---

had 80 years to run. Taxpayer contended that the rental fixed by the lease was excessive and that the purchase price of the land, which was influenced by the lease obligation, was similarly so. The Court of Appeals held that the fair value of the land was $200,000 and that the difference between this amount and the purchase price might be deducted as a business expense of the year 1941. See discussion of case in Note, 48 Col. L. Rev. 965.

[4] *Hort v. Commissioner*, 313 U.S. 28, cited by taxpayer (Br. pp. 12, 14), is similarly inapposite. There, the sum of money which taxpayer-lessor received upon the cancellation of a lease was held to be in lieu of rent and taxable as ordinary income. But the taxpayer there had sold no capital asset and was in an entirely different position from that of the lessor which made the sale to taxpayer here.

question and that it will be sound economics for him to buy out the landlord. Accordingly, he strikes a bargain with the landlord and buys the fee, thus extinguishing the lease.

In A's case, it is apparent that the expense incident to securing a release is identified with the tax year in which the settlement is made. It is a necessary expense, in the nature of damages, incurred at the time of settlement. From that point forward, A will have no further connection with the property.

In *B*'s case, however, the tenant is not severing his connection with the property. On the contrary, *B* is increasing his interest in the property so that he will have the incidents of full ownership rather than the lesser rights of a tenant for a term of years. In this circumstance, there appears to be no sound reason why his purchase of the fee should be treated differently from the case of anyone else who buys a piece of productive property or an interest in such property. It may be that the nature of *B*'s business was such that he had special need for the particular site and that the landlord was, therefore, able to obtain a higher price in selling the fee to *B* than he would have been able to secure from a third party. It can hardly be suggested, however, that a portion of *B*'s investment in the fee should, therefore, be deemed a business expense chargeable to the year the purchase was made. The tax laws must proceed upon the basis of certain objective facts. If the asset purchased is of a kind that the benefits which

the purchaser derives therefrom will extend far beyond the taxable year, the expenditure must certainly be treated as a capital expenditure, irrespective of the motives and other intangible factors which led the buyer to make the particular purchase at the particular price at the particular time.

The same is true in the instant case. In April 1945, taxpayer voluntarily renewed a lease, thereby obligating itself, under the terms of the agreement, for a 21-year period. Less than a month later, taxpayer bought out the landlord. Stated more fully, taxpayer, which was obligated to pay rental of nearly $2,500,000 over a 21-year term, purchased for $2,100,000 fee to the land upon which there was a building erected at a cost of $3,000,000. Taxpayer thereby acquired ownership of the fee and of a building having a remaining useful life of thirty years. Yet, it is taxpayer's position (at least in its most extreme form) that, except for the value of the unimproved land, this expenditure is to be deemed a business expense entirely attributable to the year 1945.

Taxpayer says in substance that it executed the renewal, notwithstanding the fact that it deemed the ground rental high, because otherwise it would have been required to abandon the valuable building appurtenant to the land. But this fact, which may be conceded, serves only to underscore the correctness of the Court of Appeals' decision: that taxpayer was buying two things—title to the land and a valuable reversionary interest in the build-

ing. As to the land, taxpayer recognizes that the value which it represents must be treated as a capital expenditure. As to the amount which is allocable to the building, the Court of Appeals held that it could be depreciated over the remaining depreciable life of the building. The holding that this amount shall be spread over that period, and not deducted in the year 1945, rests on the incontestable proposition that taxpayer has acquired the right to use the building for the rest of its useful life. Under the decision, taxpayer, like any other owner, will be able to deduct, each year, the wear and tear upon the building for that year, and it will report undistorted income. Taxpayer's contention, if upheld, would result in gross distortion of income, not only in the year of purchase, but in subsequent years as well. For if the amount allocable to the building is deducted in 1945, the effect would be the same as if one were to depreciate overnight a property interest which will actually depreciate in value (so far as one can reasonably estimate) over the course of thirty years.[5]

Taxpayer cites cases holding that a lump-sum payment may include both a business expense and a capital expenditure, but none of these cases involves facts similar to those here.[6] Moreover, there

---

[5] Taxpayer's theory would similarly distort the cost basis of the property in the event of a resale.

[6] See *Commissioner* v. *Stuart Co.*, 195 F.2d 176 (C.A. 9th), in which a payment in settlement of litigation was divided into a payment for a trade-mark (capital expenditure) and payment for canceling a contract to distribute vitamins; *Lomas & Nettleton Co.* v. *United States*, 79 F. Supp. 886 (D.

is nothing in *Commissioner* v. *Moore*, 207 F. 2d 265 (C.A. 9th), certiorari denied, 347 U.S. 942, to sustain taxpayer's contention that it incurred any deductible business expense in connection with its purchase. The taxpayer there, who had been half owner of the leased property for some years, inherited the other half from her mother. She contended that the element of value attributable to the fact that the outstanding lease was favorable at the time she inherited the remaining interest should be amortized over the period of the lease. The court held that if the lease was in fact a favorable one such favorable aspects were a wasting asset and could be amortized. In so holding, it treated the taxpayer's inherited interest like a purchase of a lease and considered such interest as a capital asset separate from the interest in the land. But see *Friend* v. *Commissioner*, 119 F. 2d 959 (C.A. 7th), certiorari denied, 314 U.S. 673. In the instant case, under the Court of Appeals' decision, the asset which may be regarded as a wasting asset, *i.e.*, the building, may be similarly depreciated over its life span.

In summary, the essence of the present case is this. Taxpayer has made an investment which gives it additional and substantial property inter-

---

Conn.), involving a sum paid by taxpayer to a receiver for certain assets and for expenses incurred by the receiver in settlement proceedings; *Olympia Harbor Lumber Co.* v. *Commissioner*, 30 B.T.A. 114, in which a lump sum paid by taxpayer was found to be payment for certain equipment and for cancellation of a business contract involving the performance of work for taxpayer.

osts. It may be assumed, as taxpayer in substance asserts, that it was to taxpayer's advantage to end its long-term lease obligation and to become an absolute owner of land and building. The fact remains that the savings represented by this advantage will be realized over the course of years. It follows that the expenditure which converted taxpayer's interests to ownership interests must be treated as capital in nature and as subject to the ordinary rules governing depreciation.[7]

II

The Court of Appeals Correctly Held that the Portion of the Purchase Price Allocable to the Building Is To Be Depreciated Over the Period of the Building's Remaining Useful Life

Accepting, *arguendo*, the Court of Appeals' holding that the entire purchase price represented a capital investment, taxpayer argues, alternatively, that it is entitled to amortize the portion of the investment allocable to the building over the unexpired period of the extinguished lease (approximately 21 years).[8] The Court of Appeals held, we

---

[7] If one assumes, *arguendo*, that taxpayer paid more than a third party would have paid, it would seem that to this extent, taxpayer was capitalizing its lease obligations in the course of acquiring the additional property interests. But the conclusion that it was making a capital expenditure remains unchanged.

[8] As observed above (note 1, p. 6), taxpayer appears to assume in its brief that this dollar amount has been determined. The Court of Appeals held, however (R. 19), that "[c]n the present state of the record we cannot determine how much of the $2,100,000 purchase price is properly to be allo-

believe correctly, that the amount allocable to the building is to be depreciated over the remaining life span of the building (30 years).

We note, at the outset, that taxpayer's contention, if accepted, would lead to absurd results. Taxpayer made the investment which gave it unlimited rights in the building in May 1945, one month after it renewed the lease for a 21-year term. Let us suppose for the moment, however, that taxpayer had made the purchase, on the same terms, in March 1945, one month before the original term of the lease expired. This would mean, on taxpayer's theory, that the added investment in a building with a remaining useful life of 30 years would be deducted as depreciation in a single year.

When one buys a capital asset (or an interest in a capital asset) which has a remaining useful life of 30 years, it follows, by definition, that it should be depreciated over that period. The depreciation allowed by the Code is "a reasonable allowance for * * * exhaustion, wear and tear." (Sec. 23(l), *supra*, p. 3.)

If *A* is a lessee of land for a term of years and he erects a building on the premises which will outlast the lease and revert, at the expiration of the term, to the landlord, he is, of course, entitled to amortize the cost of the building over the term of

---

cated to the land and how much to the building." It accordingly remanded for a determination on this point. Since it is plain that this determination should be made by the Tax Court, we address ourselves solely to the question whether the amount ultimately determined to be allocable to the building is to be spread over the 21- or the 30-year period.

the lease.[9] In such circumstances, the tenant's right to use the building is necessarily limited by the prescribed term of years and it is of no avail to him that the building will last longer than the lease term. But taxpayer here, by its added investment, changed its position from that of one whose rights of enjoyment are limited in time to that of one who has the full and perpetual rights of ownership. The additional investment in the building gives taxpayer the right and the opportunity to use the building so long as it remains usable. And the benefits or savings incident to ownership will be realized over this span.[10] Cf. *Cassatt* v. *Commissioner*, 137 F. 2d 745, 749 (C.A. 3d.), and *Post* v. *Commissioner*, 109 F. 2d 135 (C.A. 2d).

Bell v. *Harrison*, 212 F. 2d 253 (C.A. 7th); *Clara Hellman Heller Trust No. 7610* v. *Commissioner*, 7 T.C. 556, and *Miller* v. *Commissioner*, 10 B.T.A. 383, cited by the taxpayer, offer it no support. Indeed, so far as pertinent here, these cases are in accord with the decision below. In each, it was held that sums paid to acquire the use of property for a given period might be amortized over that period. Here, taxpayer, before making the pur-

[9] In this case, the original $3,000,000 cost of erecting the building was amortized by taxpayer over the 21-year period of the original lease term. (R. 49.) This was in accord with *Bonwit Teller & Co.* v. *Commissioner*, 53 F. 2d 381 (C.A. 2d), certiorari denied, 284 U.S. 690.

[10] Note that if taxpayer had continued under the renewed lease for the balance of the 21-year term, it would have been faced, at the end of that period, with the necessity of making a further arrangement with the landlords or of abandoning the still useful building.

chase, had the right to use the property for a period of 21 years. Through the purchase it acquired the right to use the depreciable property, the building, for a longer period. The longer period was the remaining life of the building, 30 years, over which the court below has held it may be depreciated.

CONCLUSION

For the foregoing reasons, the decision of the Court of Appeals is correct and should be affirmed.

Respectfully submitted,

SIMON E. SOBELOFF,
Solicitor General,
H. BRIAN HOLLAND,
Assistant Attorney General,
RALPH S. SPRITZER,
Assistant to the Solicitor General,
A. F. PRESCOTT,
LOUISE FOSTER,
Attorneys.

JANUARY, 1956.

U. S. GOVERNMENT PRINTING OFFICE 1956